1. INTRODUCTION

Family firms, where the family controls the business through significant involvement in ownership and management positions (Sciascia & Mazzola, 2008), comprise 85% of all small and medium-sized enterprises (SMEs) in the EU and the USA (Kontinen & Ojala, 2011a, p. 133), and, in turn, SMEs account for two-thirds of all businesses globally (Family Firm Institute, 2014). In this important business sector, however, research has been unable to explain satisfactorily *why some family SMEs prefer to focus on local markets and stability* (Kontinen & Ojala, 2011b), *while others may be more dynamic, striving for international opportunities* (Eddleston, Kellermanns & Zellweger, 2012).

Certainly, family SME research has identified the strategic decision to *hire professional managers* from outside the family as being crucial, recognizing the importance of their talent and skills (e.g. knowledge of customer attitudes, business practices, distribution channels, languages, marketing strategies and exporting documentation and procedures) for entry into foreign markets (Benavides-Velasco, Quintana-Garcia, & Guzman-Parra, 2013; Graves & Thomas, 2006; Stewart & Hitt, 2012). However, this key strategic choice, i.e. whether to seek managerial professionalization via external managers recruited from outside the family, cannot be seen as a stand-alone decision but needs to be considered within the whole family SME governance mechanism (Huse, 2000).

It is well recognized in the literature that family firms are heterogeneous in their governance structures (Corbetta & Salvato, 2004; Siebels & Knyphausen-Aufseß, 2012). For example, levels of ownership and management may vary (Chrisman, Chua, Pearson, & Barnett, 2012) to produce different types of firm (Miller, Minichilli, & Corbetta, 2013; Nordqvist, Sharma, & Chirico, 2014) that, in turn, may act differently with respect to their internationalization (i.e. Graves & Thomas, 2006). In this paper we argue that only a consideration of the separate and combined effects of family ownership and management (both from within the family and externally hired professionals) can better explain the internationalization outcomes of family SMEs.

However, these effects are not straightforward since research on family SME internationalization has turned out to be rather complex, both theoretically and empirically. Family firms represent contested terrain for governance paradigms such as agency, stewardship and Socio-Emotional Wealth (SEW) theories that have

generated contrasting theoretical predictions for family ownership and control (i.e. Gomez-Mejia, Campbell, Martin, Hoskisson, Makri & Sirmon, 2014; Miller, Le-Breton-Miller, Lester & Canella Jr., 2007). Empirical studies have in turn reflected these theoretical contradictions. Whereas some studies have concluded that family ownership and control have a positive impact on the internationalization of a business (e.g. Zahra, 2003), others have argued that these family-related factors have a negative effect on a firm's international activities (e.g. Fernández & Nieto, 2006; Graves & Thomas, 2006; Majocchi & Strange, 2012; Muñoz-Bullon & Sanchez-Bueno, 2012). Some studies have even detected no significant influence (e.g. Merino, Monreal-Pérez, & Sánchez-Marín, 2014). These apparent contradictions may have been to some extent the consequence of the empirical decision in the majority of studies (e.g. Cerrato & Piva 2012; Fernandez & Nieto, 2005) to use a dichotomous (family versus non-family) categorization of family SMEs.

Building on George, Wiklund, & Zahra (2005, p. 210) who concluded that governance structures "…influence the proclivity to take risks and expand the scale and scope of [SME] internationalization efforts", this paper argues that we need to reconsider and overcome this family/non-family dichotomy (Gomez-Mejia et al., 2014) in order to increase our understanding of the separate and combined impact of ownership and management on family SME internationalization. As a further empirical refinement we propose an improved entropy measure of family SME internationalization based on its scope rather than its volume.

Our paper proposes these empirical improvements and offers a possible resolution of the contested theoretical terrain that has been identified by focusing on the interaction between governance (ownership) and management (strategy to hire outside managers) and their joint influence on the strategic outcome of internationalization. We propose a new and integrative theoretical framework based on a synthesis of theories of corporate governance in relation to family ownership, and theories of social capital for external managerial hires. We argue that this synthesis is necessary for the generation of nuanced hypotheses concerning the full impact of family ownership and control.

To test these hypotheses we base our empirical analysis on a sample of 417 Italian manufacturing family SMEs, and address governance and strategy (and their interaction) in a context where ownership patterns are relatively simple, and information about strategies (e.g. hires of outside managers) is relatively easy to

access and assess, compared to large firms (Siebels & Knyphausen-Aufseß, 2012) demonstrating the importance of this interaction to explain governance-strategy-performance in family SMEs. In other words, we are able to analyze this theoretical sequence with family firms in a way not possible with larger firms.

Our paper contributes to the general SME internationalization literature and to the nascent literature on the internationalization of family SMEs (Calabrò, Torchia, Pukall, & Mussolino, 2013; Kontinen & Ojala, 2010, 2011a, 2011b; Liang, Wang & Cui, 2014; Merino et al., 2014; Pukall & Calabrò, 2014; Segaro, Larimo, & Jones, 2014; Sciascia, Mazzola, Astrachan & Pieper, 2012) by analyzing the diversity of governance mechanisms in family SMEs as a potential explanation for some of the mixed and often contradictory results (Chrisman et al., 2012). We present theoretical explanations of our findings, and explain how prior, inconsistent studies may be reconciled in a field where "…empirical verification is needed" (Sharma, 2004, p. 15).

2. THEORETICAL BACKGROUND

The analysis of the effect of outside managers and ownership on the internationalization of SMEs in general, and family firms in particular, involves social capital theory and competing variants of theories of corporate governance. Prior research has used social capital to explain how SMEs access resources to succeed internationally (e.g. Agndal, Chetty & Wilson, 2008), and corporate governance theories to investigate the effects of ownership on internationalization (e.g. George et al., 2005). The first theoretical lens helps us to frame the inclusive role played by external managers in bridging SMEs to external resources, and the second allows us to analyze the relationships between owners and managers and the impact of these relationships on internationalization.

2.1 Social Capital

"*Social capital* is the contextual complement to human capital" (Burt, 2000, p. 347). While human capital refers to the quality of an individual, social capital refers to the relationships created between people (Burt, 1999). These represent the "actual or potential resources" (Bourdieu, 1986, p. 248) that a firm can "…access and/or mobilize in purposive actions" (Lin, 2001, p. 12). Adler & Kwon (2002) define social capital, therefore, as the relationships between individuals and organizations that

facilitate action and create value, or "...the goodwill and resources made available to an actor via reciprocal, trusting relationships..." (Arregle, Hitt, Sirmon & Very, 2007, p. 73). We find these relationships within an organization (internal social capital) and/or between an organization and its external parties (external social capital) (Nahapiet & Ghoshal, 1998). With the limited resources of SMEs in general, research has shown social capital to be a significant influence on their internationalization (Chetty & Pahlberg, 2015; Kontinen & Ojala, 2011b; Musteen, Francis & Datta, 2010; Prashantham & McNaughton, 2006; Zhou, Wu & Luo, 2007), and many scholars (e.g. Agndal et al., 2008; Presutti, Boari & Frattocchi, 2007; Yli-Renko, Autio & Tontti, 2002) have argued that SMEs rely heavily on external relationships to acquire information and gain access to foreign markets.

No firm may control all of the resources that it needs to compete in the marketplace and networks (as a resource) are not independent of other resources. In relation to financial capital, for example, Toms & Filatotchev (2004) emphasize the network contacts that may become available when firms admit outside investors, particularly when outsiders are given seats on the board (Majocchi & Strange, 2012); similarly, the recruitment of outside managers may facilitate access to their network contacts, introducing improved knowledge of the industry, cognitive diversity and environmental scanning (Hatum & Pettigrew, 2004). This paper argues (see below under Hypotheses) that social capital theory explains the importance of externally-recruited managers to family firms, mainly through their combination of bonding and bridging social capital. However, managerial selection and ownership characteristics are not just independent processes but represent two faces of the same coin, especially in the context of family SMEs, where ownership is key to the control of managers and could facilitate or hinder the social capital of outsiders (Burt, 2000, p. 399). Put differently, the social capital brought by outsiders (i.e. external managers) could be contingent on the firm's ownership structure and/or subject to the positive or negative perceptions of the owning family (De Massis, Kotlar & Frattini, 2013). We therefore synthesize social capital with corporate governance theory that stresses the importance of the interaction between the presence of outside managers and ownership distribution. We develop this second, complementary approach to family firm internationalization in the next section.

2.2 Corporate Governance

SMEs and family firms are mainly distinguished by their unique corporate governance, or the means by which managers are controlled (Shleifer & Vishny, 1997), and theories of corporate governance are contested terrain inhabited by agency, SEW and stewardship theories.

An *agency* perspective has dominated most family firm research, with its focus on contractual arrangements and its assumption of opportunistic parties constrained by governance institutions (Eisenhardt, 1989). For example, firms owned by outside shareholders must resolve Jensen & Meckling's (1976) "divorce" of ownership and control. Outside shareholder principals and salaried, non-family managerial agents introduce the familiar problems of moral hazard and adverse selection. We refer to these costs as "Type I" agency costs or principal/agent problems.

One important means of coping with Type I agency problems involves blockholders or strategic investors (Singla, Veliyath & George, 2014). Blockholders are typically defined as shareholders owning a large fraction of the firm's equity, (Denis, Denis & Sarin, 1999) who therefore have an incentive and power to monitor managers in a vertical hierarchy. Indeed, families with their concentrated ownership and tight control constitute the ultimate blockholders, attenuating Type I costs since family owners are incentivized to monitor themselves (and others) as managers, i.e. with self and horizontal monitoring rather than through vertical supervision (Bainbridge, 2012).

However, outside ownership in family firms (i.e. family ownership with control less than 100%) may theoretically re-introduce the separation of managers and owners and also "Type II" (or principal/principal) agency problems: where minority investors have weaker incentives to monitor managers and outsiders also run the risk of being exploited by other investors with bigger stakes and who may enjoy private benefits from their control (Faccio, Lang & Young, 2001). Of course, we can view these private benefits as attractive sources of SEW (as discussed below) by families, but also as Type II agency costs by outside investors. Family shareholders with salaried managerial positions may reduce Type I agency costs but we may also perceive them as being under-diversified, with all their "eggs in one basket" in relation to their human capital and financial investments. Such trade-offs between negative costs and positive benefits are typical of theories of family governance, where net outcomes may depend empirically upon local circumstances.

At the same time, the corporate governance literature has developed softer, less cynical and more "socialized" theories of family governance. Like agency theory, however, they can yield negative as well as positive predictions. *SEW theory* (Berrone, Cruz & Gomez-Mejia, 2012; Gomez-Mejia, Cruz, Berrone & De Castro, 2011) emphasizes reputational and affectional (i.e. non-financial) values (Arregle, Naldi, Nordqvist & Hitt, 2012), where family members derive utility from family influence and identification with the firm, with future generations of the family taken into account, i.e. "…creating a legacy" (George et al., 2005, p. 214). In other words, families enjoy the benefits that agency theorists see as costs from the shareholders' point of view.

SEW theorists (e.g. Gomez-Mejia et al., 2011) take a balanced view of these benefits and costs. For example, compared with non-family employees and shareholders, family members have their financial and human resources locked in and cannot easily exit the family firm. This means that their internal voice may replace their exit threat, and this parallels the self- and horizontal monitoring of agency theory, with the monitoring of managers carried out by themselves or by peers rather than by superiors, e.g. shareholders. We may perceive human resource management practices to be more generous and positive in family firms from an SEW perspective, but management succession decisions may still disregard professionals from outside, with negative consequences (Gomez-Mejia et al., 2011).

S*tewardship theory* (Miller et al., 2007) views family members as being closely attached to their firm and acting as responsible stewards for the whole business. This approach extends the SEW perspective beyond the family to embrace other stakeholders besides family members. Thus, governance based on stewardship may lead to higher and longer-term investments in relations with customers, lenders and employees, and access to "patient" long-term capital (Sirmon & Hitt, 2003).

In contrast with SEW and stewardship theories, an agency perspective considers that the family preferences identified by these theories are costly, not beneficial, leading to nepotism and the entrenchment of families (Burkart, Panunzi & Shleifer, 2003). Where family assets have a financial and non-financial value, Verbeke & Kano (2012) identify a "bifurcation bias" in family firms towards SEW promoting investments, which are in their view dysfunctional.

What do these mixed perspectives mean for the specific outcome of internationalization in the context of family SMEs? In Table 1 we use the distinction

between family-influenced and family-controlled SMEs (Sirmon, Arregle, Hitt & Webb, 2008; Arregle et al., 2012) to summarize the theoretical effects on internationalization of different degrees of family ownership (i.e. low or high family ownership), and management (i.e. family managers only, or of family members *and* externally recruited managers). We argue that the efficiency effects of external managerial recruitment will depend on whether a family firm is unilaterally controlled (i.e. the family has majority ownership >50%) or just family influenced (i.e. the family is the main shareholder but where the family does not have unilateral control <50%).

TABLE 1 NEAR HERE

Although we couch Table 1 in general terms, with the signs on its elements viewed from an agency, economic efficiency perspective, it is easy to interpret in the context of internationalization. Table 1 shows that we may associate high (>50%) levels of family ownership combined with some family representation in decision-making with many negative effects (quadrants 2 and 4). In terms of internationalization, Type II agency problems may be high, and international projects resisted; under-diversified, relatively loss-averse family members may oppose internationalization, arguably involving additional costs/risks. In this type of firm, controlling family owners may exploit outside shareholders by pursuing strategies for their own benefit, rather than for all shareholders (i.e. Type II agency problems). This means that they may overlook profitable opportunities in international markets if they do not offer improved SEW for the family. In addition, SEW theory would predict family resistance to external ownership and capital that dilute their own stakes, and a preference for conservative decisions that favor local stakeholders (employees and customers) rather than international ones.

The only positive arguments in favor of internationalization by SMEs with unilateral family control (quadrants 2 and 4) would emphasize the attenuation of Type I agency costs with family owner-managers and their access to patient capital with a long-term perspective, possibly leading to long-term investments in international markets. However, agency theorists would see even such long-termism as counter-efficient, and family members with unilateral control are likely to impact negatively on strategies like internationalization that may lead to higher levels of risk (Gentry,

Dibrell & Kim, 2014) because they may depend on the firm for their employment, their long-term personal and family wealth, (Sirmon & Hitt, 2003) as well as their SEW, and this may discourage them from seeking internationalization involving further resource commitments. In the context of this paper, "…the preservation of SEW is purported to affect diversification strategies" (Sanchez-Bueno & Usero, 2014, p. 1312). Overall, our analysis suggests that when firms are family-controlled, the positive effects of hiring external managers are absent, and Type I and II agency costs remain high (quadrant 4).

In contrast, in quadrant 3, we may expect family-influenced SMEs (with <50% family ownership and with family and external managers), to generate a predominance of positive attitudes towards internationalization from external shareholders and managers. A growing stream of literature (Anderson & Reeb, 2004) argues that this type of firm may combine the benefits of minority family ownership with only a few of the negative side-effects of unilateral control. In other words, allowing "other voices at the table" (Sirmon et al., 2008) may generate a positive internal dialogue between different stakeholders. At the same time the firm may preserve close links between family shareholders and managers to a large degree.

In this kind of firm, while all the positive aspects of family firms remain in place, a more plural composition of shareholders may mitigate their main weaknesses. The presence of majority outside shareholders reduces the total identification of the firm with the family, limiting Type II agency problems, e.g. the extraction of private benefits such as personal loans to family insiders, appropriation of corporate opportunities or excessive compensations (Shleifer & Vishny, 1997). All of these behaviours may divert resources away from the more profitable business opportunities that may arise in foreign markets. While family dominance is less pronounced, family values may remain at the core of business strategies, but a more balanced approach to internationalization could emerge from a mix of different perspectives on boards.

It can be seen from this theoretical background, therefore, that theories of social capital and corporate governance both generate strong presumptions in favour of the hiring of external professional managers by SMEs, and particularly family-influenced firms, in the context of internationalization. The conditions under which this assumption holds true are discussed in the next section, where we use our theories together to generate hypotheses, supported by relevant, extant empirical findings.

3. HYPOTHESES

Although "…SMEs typically rely more extensively on network relationships as they pursue international opportunities" (Musteen et al., 2010, p. 197), the trouble with family firms (85% of SMEs) is that "…networks both facilitate and constrict internationalization by SMEs" (Musteen et al., 2010, p. 203). Family SMEs typically possess strong internal, or "bonding", social capital, i.e. socially homogeneous relationships with other members of the firm but lack external, heterogeneous "bridging" relationships (Prashantham & McNaughton, 2006; Schuller, Baron & Field, 2000). In this context, family ties within family firms represent an extreme form of bonding social capital – or "family capital" (Kontinen & Ojala, 2011a, p. 134; Hoffman, Hoelscher & Sorenson, 2006) – that brings family members together, probably having the same set of shared norms and values. In this case the two forms of social capital – the family's and the firm's – coexist (Arregle et al., 2007; Lansberg, 1983).

However, activities in foreign markets may require specific external social capital in the form of managerial knowledge and capabilities. Marketing strategies must be adapted to new market conditions and the management of a firm's finances and risks typically become more complex. In short, internationalization, even if only in the relatively simple form of exports, requires specialized and professional management (Sciascia et al., 2012). This is even truer when firms sell in many different countries. In this case the diversity of national contexts in terms of consumers' behaviors, legal and administrative requirements, and market conditions increase significantly the complexity that managers should handle. This in turn sets the bar higher for SMEs that need specific additional expertise, experience and networks to address the increased complexity.

In family SMEs, however, managers are typically family members (Wilson, Wright & Scholes, 2013), and a steady stream of literature (e.g. Classen, Carree, Van Gils & Peters, 2014; Bennedsen, Nielsen, Perez-Gonzalez & Wolfenzon, 2007) has reported that family management may be detrimental to firm performance, and to internationalization. This literature proposes that restricting managerial selection to the family severely limits the potential quality of the management team. Moreover, Bloom & Van Reenen (2007) highlighted the existence of what they called the "Carnegie effect", i.e. the limited investments in education and training by family

members who can rely on a guarantee that they hold lifetime management positions. If family firms recruit internally, this is likely to add others to the management team who are similar in terms of networks and contacts (Arregle et al., 2007; Prashantham & McNaughton, 2006). This all suggests that family SMEs are likely to have to recruit outside professionals in order to increase the scale and scope of internationalization.

In terms of social capital, outside managers and "…bridging ties may foster novel ideas, knowledge and opportunities that are valuable to internationalizing SMEs; yet, they tend to be geographically distant and difficult to access" (Prashantham & McNaughton, 2006, p. 448). They go on to consider bridging ties with local multinational enterprises but in the context of this paper, the hiring of outside professionals may constitute an alternative opportunity for the acquisition of bridging social capital, and particularly access to knowledge of internationalization, which could be internalized and bonded within the firm.

Therefore, the hiring of external managers plays a double function, avoiding, on one side, the managerial entrenchment that is typical of family firms (Gallo & Vilaseca, 1998) and providing, on the other hand, a new, diverse source of managerial knowledge in the form of additional experience and expertise plus additional contacts and relationships. This overlap of networks between the family and the external managers may enrich the firm's overall social capital (Jack, 2005; Arregle et al. 2007), and may in turn enhance its ability to develop a stronger and more diversified internationalization. The theoretical arguments presented above establish a strong presumption in favor of hypotheses predicting positive relationships between external managers and internationalization. So in line with the prediction of social capital theory that external managers may be an efficient local source of bridging social capital, and have broad knowledge of international business, we hypothesize that:

H1 - In family SMEs, there is a positive relationship between the presence of external managers and internationalization.

H1 is not new, however, and, as reported in the introduction, empirical testing to date has variously concluded that family managers have a positive impact on the internationalization of a business (e.g. Zahra, 2003), while others have found that these family-related factors have a negative impact (Fernández & Nieto, 2006; Graves

& Thomas, 2006; Majocchi & Strange, 2012; Muñoz-Bullon & Sanchez-Bueno, 2012). Some studies even detect no influence at all (Merino et al., 2014). Sciascia et al. (2012) estimate for international entrepreneurship an optimal mix of family involvement in the management team, involving a high proportion of outsiders, while Majocchi & Strange (2012) find that external board members are associated with increased levels of internationalization. Some of these contradictory results may be the consequence of the dichotomous (family versus non-family) ownership categorization of family SMEs that is prevalent in the majority of studies (e.g. Cerrato & Piva 2012; Fernandez & Nieto, 2005) and confirmed by recent meta-analyses (Machek, Hnilica & Brabec, 2014; O'Boyle, Pollack & Rutherford, 2012).

This paper argues that the family/non-family firm dichotomy needs to be reconsidered in the context of interaction with external managers: there is an infinite number of combinations of family ownership and family control, and the main thrust of this paper is that the impact of non-family managers depends on the concentration of family ownership (Calabrò et al., 2013; Yang, 2010), where corporate governance theories explain how outside ownership and outside management may interact. An inspection of quadrant 3 in Table 1 shows that majority outside ownership may amplify any positive effects of the presence of external managers. Majority outside ownership could conceivably introduce certain Type I agency problems, but if external shareholders support externally recruited managers in their decisions, Type II agency costs will be lower compared to quadrant 4. External shareholders may reduce bifurcation bias (Verbeke & Kano, 2012) and they are also likely to be more diversified than family owners, implying less loss aversion and opposition to internationalization; outside owners may be less emotionally attached to local stakeholders and, finally, there may be less hostility towards obtaining the external finance necessary for internationalization. In family-influenced SMEs (with minority family ownership <50%), the presence of outside investors shifts the nature of "mixed gambles" in favour of more investment in costly/risky projects (Gomez-Mejia et al., 2014) where external professional managers can fully exploit their networks, knowledge, talent and skills to successfully manage entry into foreign markets. In other words, family-influenced SMEs allow social capital resources to play their crucial competitive role (Pearson, Carr & Shaw, 2008) and these firms are more likely to exhibit lower loss aversion and to recognize the potential for further gains from internationalization.

To summarize, it is quadrant 3 in Table 1 that represents the dominant positive consequences of the presence of external managers in family-influenced SMEs compared with family-controlled ones. We therefore propose a second hypothesis:

H2 – The effect of the involvement of external managers on internationalization depends on the level of family ownership and it will be more positive for family-influenced (low level of family ownership) than for family-controlled SMEs.

4. DATA AND METHODOLOGY

4.1 Data

Our empirical work is based on the ninth and tenth waves of the Italian "Survey of Manufacturing Firms" collected by Capitalia (now UniCredit, the largest Italian bank by assets) in 2004 and 2007. This bank collected the data from a large sample of manufacturing firms over a period of six years (2001-2003 for the ninth wave and 2004-2006 for the tenth wave), and the bank triangulated its survey responses with data held in the AIDA database (part of the Bureau Van Dijk) and the CEBI database (originally set up by the Association of Italian Chambers of Commerce). This triangulating procedure increased sample reliability and overcame the methodological limitations of using self-reported surveys as the only source. The initial balanced panel dataset provided by the bank for the two survey waves comprised 1,049 Italian manufacturing firms (UniCredit, 2008).

Of course, even the most ardent advocates of archival data must concede that current researchers can have no control of data collected in the past (Hughes & Goodwin, 2014), but we would argue that these surveys represent a vital archival resource, professionally collected from very large samples of firms. The use of the same archival secondary dataset by other scholars in previous published works (e.g. Cerrato & Piva, 2012; Hall, Lotti & Mairesse, 2009) is also a further sign of the reliability of our data source and it allows comparability of our results.

We focused our analysis on unlisted firms with 11-250 employees, thus complying with the European Commission (2003) definition of SMEs. This lead us to a balanced panel consisting of 736 Italian manufacturing SMEs. We concentrated on manufacturing SMEs for three reasons. First, the Italian industrial system is largely dominated by manufacturing SMEs (European Commission, 2009). Second, we considered exports, which are the typical internationalization mode for manufacturing

but not services SMEs. With the intangibility and inseparability of services, production and distribution activities may overlap so that sales to foreign clients may require that either the firm or the clients must relocate (Blomstermo, Sharma & Sallis, 2006), so service exports are often not a significant indicator of internationalization (Czinkota, Grossman, Javalgi & Nugent, 2009). Third, Italy is a very interesting setting for analysing manufacturing exports, as the second largest manufacturing country in Europe after Germany and the eighth largest manufacturing exporter in the world (World Bank, 2015).

In order to select our sample of family SMEs we referred to previous studies (Chua, Chrisman & Sharma, 1999; Zahra, 2003) where family involvement in both ownership and management distinguishes family firms. Research has measured family ownership as the percentage of equity held by family members, and family involvement in management as the number of a firm's managers who are family members (e.g. Chua et al., 1999; Sciascia & Mazzola, 2008). From our sample of 736 Italian manufacturing SMEs we had to remove 90 observations as firms did not report information on the type of management (family or externals). In our reduced panel of 646 Italian manufacturing SMEs, families owned 458 firms (70.9%), i.e. the largest shareholder was a family member. However, we considered only 418 (64.79%) to be family SMEs, where family members were also managers. We only considered 417 of these family SMEs for analysis in relation to our dependent variable, as explained below.

The average percentage of family ownership in our sample of 417 family SMEs was 51.4% (SD 24.1%). This is in line with prior studies on family SME internationalization that define family SMEs in terms of a majority (>50%) of shares in family hands (i.e. Graves & Thomas, 2006), with one or more family members in managerial positions (i.e. Fernandez & Nieto, 2006).

Besides the percentage of family ownership, we also distinguished family SMEs into family-controlled and family-influenced SMEs, following Sirmon et al. (2008) and Arregle et al. (2012): family-controlled firms had family ownership >50% and at least one member of the family was involved in the management team; in a family-influenced firm, family ownership was <50% and at least one family member of the management team. Accordingly, the number of family-influenced SMEs in our sample was 254 (out of 417, i.e. 60.9%) and family-controlled SMEs were 163 (39.1%). The average family ownership shares in a family-controlled and family-

influenced SME were 76.3%, and 36.4% respectively.

4.2 Variables and Measures

4.2.1 Dependent variable

Previous studies have mainly employed the most common measure of the scale of SME internationalization, i.e. the ratio of foreign to total sales (FSTS), equivalent to export intensity if the latter includes the local sales of overseas representative offices, subsidiaries, etc. as a dependent variable (Katsikeas, Leonidou & Morgan, 2000; Lu & Beamish, 2001; Westhead, Wright & Ucbasaran, 2001). However, while this provides one simple measure of the scale of internationalization, it does not provide a fine-grained measure of its scope. Indeed Rugman & Verbeke, (2004) proposed the geographical distribution of sales as a complementary measure of internationalization. For example, two firms may show similar export intensities, but one could export to a single neighbouring country, while a second had sales to many countries over three continents. With similar export intensities, the levels of complexity to be managed could be quite different, so a count measure of export destinations has complemented export intensity (George et al., 2005). However, this measure does not account for the different weight of sales in different countries. The entropy measure addresses specifically this limitation by considering jointly the number of countries and the distribution of exports. This measure derives from the entropy index which measures firms' product diversification (Jacquemin & Berry, 1979) and lately a firm's international diversification (Gomez-Mejia, Makri & Kintana, 2010; Hitt, Tihanyi, Miller & Connelly, 2006; Majocchi & Strange, 2012; Sanchez-Bueno & Usero, 2014). Therefore, we used this entropy index to measure international diversification (or scope) as our preferred *dependent variable*.

In order to develop this entropy variable we considered the geographical distribution of sales to ten different areas: domestic, the Euro Zone, other countries within the EU, other non-EU European countries, China, other Asian countries, Africa, North America, Latin America and Oceania. Using this classification, we calculated our measure of international diversification as:

$$\textit{Entropy measure} = \sum_{J=1}^{10} x_j \ln\left(\frac{1}{x_j}\right)$$

Here, the subscript *j* defined one of the ten different destination areas, and x_j is the ratio FSTS for that specific market *j*. The natural logarithm of the inverse of the sales realized in every market was the weight given to each geographical segment. This measure is zero for a firm with concentrated sales in just one country, and the maximum value of the measure would be 2.302 in the theoretical case of a firm with a perfectly homogeneous ratio of sales of 10% in all ten regions.

Since our sample comprises SMEs, almost all firms have domestic sales, with many having sales concentrated predominately in the domestic market. This distribution is consistent with recent findings that show that, even in a context of growing globalization, firms tend to have sales concentrated in the home and regional markets (Rugman & Verbeke, 2004), particularly family firms (Banalieva & Eddleston, 2011). Our measure of international scope takes a value of zero when a firm concentrates all its sales in one country, whether home or abroad. In this case our dependent variable would be biased (Brouthers, Nakos, Hadjimarco & Brouthers, 2009). We controlled for this contingency and found only one of our 418 family SMEs with a FSTS ratio of 100%, with only one export market, and therefore an entropy measure of zero. We dropped this case, so the final sample for our analysis was 417 firms.

As a further robustness check (see section 5.1 below) we controlled for the correlation between our entropy measure and the more traditional FSTS ratio. This correlation was quite high at .7316 ($p<0.01$) suggesting that our entropy measure proxies a similar phenomenon to the FSTS ratio, but with the additional strength of weighting the index for the number of export destinations. The case of two firms with an FSTS of 50% but with a different distribution of export clarifies the point, e.g. the first firm has all its foreign sales concentrated in one country while the second has 10% of its sales each in five different regions. While FSTS does not measure the increased complexity faced by the second firm, our entropy measure does, since the entropy index would be 0.693 for the first firm and 1.498 for the second.

In our case, the average value of the dependent variable was 0.533, ranging from zero to a maximum of 2.23, with the average value dominated by the high number of SMEs focused on domestic sales. With our sample of 417 family SMEs, 115 (27.5% of the total sample) had an entropy value of zero. This distribution of the dependent variable suggested not using Ordinary Least Squares (OLS) in our

estimation procedure. We address this issue below.

4.2.2. Independent variables

Our main *independent variable* measured the presence of external managers in family SMEs. We considered a dummy variable (*External managers*) taking the value of 1 when the family SMEs employed external managers besides family managers, and zero when the family SMEs employed only family managers, since Enriques & Volpin (2007) consider this an appropriate measure of the presence of specialist, independent executives in family firms, the number of family SMEs with external managers was 127 (i.e. 30% of 417): 77 family-influenced and 50 family-controlled. This variable *External managers* appears as the main independent variable for our Models 2, 3 and 4 in Table 5, and as the independent and *moderator* variable for our Models 5 and 6 where we interacted it with the level of family ownership.

Our second set of independent variables measure family ownership. We used two measures. First, we used a dummy variable (*Family influenced*) equal to 1 when family ownership is <50% and the management team has at least one family member, i.e. when family ownership is greater than 50% (i.e. the firm is family-controlled, and there is at least one member of the family involved in the management team) the dummy takes the value of 0. Second, we also used the percentage of family ownership in its continuous form, taking values between 0 and 100 (*Family ownership)*, and used in Models 5 and 6 respectively.

4.2.3 Control variables

We included the standard *control variables* adopted in previous research on SME internationalization's determinants (e.g. Lu & Beamish, 2001; Westhead et al., 2001). Using Pavitt's (1984) well-known taxonomy that classifies sectors according to their technological traits, we included four different industrial sectors: the *"Traditional"* sector (53.72% of firms in our sample), *"Scale-intensive"* industries (14.87%), *"Specialized-suppliers"* (28.30%) and *"Science-based"* industries (3.12%). Since the traditional sector was the most relevant category in our sample (see Table 2), we used it as the reference sector for three sector dummies.

We also identified four Italian regions with specific dummies: the *North-West* (37.41% of firms in our sample), *North-East* (29.99%), *Centre* (19.18%) and the South combined with Sardinia and Sicily (*South & Islands*) (13.43%). The North

West, our biggest region, became our reference region. Given the significant regional differences in the distribution of firm-specific location-bound advantages (Basile, 2001) we expected that this control variable would significantly influence foreign sales by family SMEs. As the firm's membership of a business group can affect the international activities of a family SME (Cerrato & Piva, 2012; Chung, 2014), we also controlled for this with a dummy variable (*Group*): unity if the firm belonged to a group (11.99% of our sample), zero otherwise.

Finally, we considered additional controls in relation to internationalization: size, age, past profitability, innovation levels and past internationalization. Following Verwaal & Donkers (2002) we represented firm size by the log of total employees (*Size*), while our sample ranged from 11 to 250 employees (mean 70.28 with a SD of 48.23). We measured a firm's experience (*Age*) by the years since foundation (Johanson & Vahlne, 1977), with an average of 31.6 years for our sample. In order to measure past profitability we used Return On Investment (*ROI*) in the year 2003 (average value 15.98%). To measure innovation, we used Research and Development (R&D) employees over the total number of employees (*R&D*) rather than an input measure of the innovation process (such as R&D expenditure over total sales) as prior studies have reported this as unreliable, particularly in an SME context (Hoffman, Parejo, Bessant & Perren, 1998). We also controlled for path dependency (Hashai, 2011) by using the percentage of foreign sales in regional markets in 2003 (*Reg_sales*). We believe that this approach also corresponds with prior literature, e.g. Banalieva & Eddleston (2011) reported a "regional" path dependency among firms characterized by a high level of family management, as in our case. We present a list of all our variables and a description of their measurement in Table 2.

TABLES 2 NEAR HERE

We report the descriptive statistics for both our binary and continuous variables in Tables 3 and 4, together with correlation indices. The low value of all the indices suggests that multicollinearity need not be a cause of concern. As a further test, we also calculated Variance Inflation Factors (VIFs) for all the variables. The average VIF value was 1.45 with a maximum of 3.06 for our interaction terms. All the VIF values are well below the usual thresholds reported in the literature (Studenmund, 1992), confirming that multicollinearity is not an issue for our analysis.

TABLES 3 and 4 NEAR HERE

4.3 Methods

Since we censored our dependent variable showing a high percentage (27.5%) of observations at the lower limit, we adopted a Tobit regression methodology (Bowen & Wiersema, 2004; Greene, 2002), frequently used in similar contexts (Merino et al., 2014; Sanchez-Bueno & Usero, 2014) in order to take into account the peculiar nature of our measure. Tobit regression coefficients estimate the linear effect on the uncensored latent variable but not the observed outcome. Therefore we may interpret these coefficients in a similar manner to OLS regression. This means that in our case, we estimate coefficients only for those firms engaged in internationalization.

We controlled for potential reverse causation from our measure of internationalization to the presence of external managers by lagging our explanatory variables by three years. In other words, we used the dependent variable for 2006 and the explanatory variables (including all the control variables) for 2003. Prior studies (George et al., 2005; Zahra, 2003) also use this approach to deal with potential endogeneity.

In order to test our hypotheses we ran a series of regressions reported in Table 5. We first tested our hypotheses on the role of external managers using the whole sample (Model 2) and then we split the sample and ran two separate regressions (Models 3 and 4), one with just family-influenced and one with just family-controlled firms. As a further test we also ran two separate regressions with interactions (Model 5 and 6). In Model 5 we interacted a dummy variable (*Family-influenced*) - the variable took the value 1 if the company was a family-influenced SME, and 0 otherwise - with the variable measuring the presence of external managers (*External managers*). We then included in Model 6 a continuous variable measuring the percentage of family ownership (*Family ownership*) to test its direct effect on a firm's international diversification (or scope), and finally we multiplied this variable by the presence of external managers (*External managers*) to capture any interaction effect. Since precise data on family ownership percentage were missing in 9 cases, the regression of Model 6 (Table 5) had only 408 observations and not 417 as in the previous Models.

TABLE 5 NEAR HERE

5. RESULTS

We report our main results in Table 5. In a Tobit regression, Pseudo R-squared is different to R-squared from the OLS regressions. We calculated McFadden's pseudo R-squared as one minus the ratio of the log likelihood of the full model over the log likelihood of the constant-only model. The values of the pseudo R-squared indicated that the predictors in our models were effective. As a further test that our model was correctly specified we ran a link test (Pregibon, 1980) using the *linktest* command in Stata and regressing, using a Tobit procedure, our dependent variable on the prediction and the prediction squared. We found a statistically significant predictor, while the prediction squared did not have any explanatory power, confirming the absence of specification problems in our model.

Model 1 in Table 5 was our baseline model that included only control variables. In Model 2 we added our main independent variable, the dummy variable for *External managers*. The coefficient was positive and significant ($p<0.1$) as expected, confirming H1 for the whole sample of family SMEs.

We report our most interesting results for Models 3 and 4 where we split our sample in two for each contingency: Model 3 shows the regression results for the sample of family-influenced SMEs, while Model 4 generates results for the sample of family-controlled SMEs. For family-controlled SMEs (Model 4) the coefficient for *External managers* was negative and not statistically significant. In contrast, the coefficient in family-influenced SMEs (Model 3) was both positive and significant at the 5% level. Overall the results confirmed our H2 that the effect of *External managers* on family SME internationalization depends on the concentration of family ownership, so that the relationship holds true for family-influenced SMEs but not for family-controlled SMEs.

We also found support for H2 in multiple tests that used the interaction terms reported in Model 5 and 6 of Table 5. Model 5 shows that ownership <50% in a *Family influenced* company *per se* does not have a positive and significant effect on family SME international scope and we report the same result for the presence of *External managers.* However, the interaction term of these two variables (*Family influenced* and *External managers*) is significant ($p<0.05$) and it has a positive sign, suggesting that the presence of externally hired managers in family-influenced firms

produced the positive effect on international scope. We also ran an additional regression (Model 6), interacting the percentage of family ownership (*Family ownership*) with the *External managers* variable. We expected a negative sign on the interaction for high levels of family ownership and the results further supported H2. In this case, *Family ownership* is not significant while the presence of *External managers* in family SMEs is positive and significant ($p<0.01$). More importantly, the interaction term has the hypothesised negative sign ($p<0.05$), suggesting that SMEs with lower level of family ownership and external managers tend to have a higher level of international scope. All these results support a synergistic relation between family influenced SMEs (i.e. with lower levels of family ownership, or openness towards external capital) and the presence of external managers.

This interaction is further illustrated in Figure 1 where we show the effects of the interaction term (i.e. *External managers* used as a *moderator*) as estimated in Model 6 of Table 5. Figure 1 reports the percentage of family ownership on the *x*-axis and the level of internationalization on the *y*-axis. The Figure shows that the level of internationalization of family SMEs with only family managers (continuous line) is higher when the level of family ownership is high (i.e. *family controlled*, i.e. external capital participation is low). On the contrary, the level of internationalization of family SMEs that employ also external managers (dotted line) is higher when the level of family ownership is low (i.e. *family influenced*, i.e. the ownership structure is more open to outside investors). In other words, the positive effects of hiring external managers on the international scope of family SMEs are evident when the ownership structure of the company is open to external capital (i.e. with low levels of family ownership). For ease of reading, we set the constant term at 0 (in the model, actually -0.894). Since we use a binary variable (i.e. *External managers*) as moderator we do not employ standardized variables (Aiken & West, 1991).

Comment [A1]: This goes against the relevant hypothesis. Internationalization should be lower in this case.

Figure 1, a graphical presentation of the interaction between family ownership and external managers on the internationalization of Italian family SMEs, presents a slope test for the regression line when firms have only family managers, which is positive and equal to 0.00132 ($p=0.335$) but insignificant. (This is the regression coefficient of the variable *Family ownership* as reported in Model 6, Table 5). The slope test for the regression line when firms also have external managers is negative and equal to -0.005 ($p=0.727$) but is also not significant. This does not represent a problem in the context of our research aim, to evaluate whether there is a significant

difference between the slopes (of the two trajectories) themselves. In our case the significance of the interaction term remains the main criterion for rejecting the null hypothesis that the coefficient term is equal to 0 and this is sufficient to support our hypothesis H2 (Dawson, 2014). Since the significance level of the interaction term in Model 6 of Table 5 is equal to -0.006 (p=0.002) and is significant, we can conclude that the effect of external managers on internationalization (*Entropy*) depends on the level of family ownership.

FIGURE 1 NEAR HERE

5.1 Robustness Check

In addition to the tests described above, we ran further robustness checks. First, we ran a Tobit analysis substituting our dependent variable entropy with the more prevalent FSTS ratio. Second, we ran our regressions using OLS with entropy and FSTS as dependent variables separately. In all cases we found results very similar to those reported here, thus further corroborating our findings.

Next, we ran additional tests for the interaction term. First, we checked that the signs and statistical significance of the interaction term, and the graphical representation obtained with OLS were consistent with our results using the Tobit methodology. Once again the results were in line with the findings already reported in Table 5. Second, following Buis (2010) we checked the differences between marginal and multiplicative effects, computing the influence on international scope for the variables external managers, and for family-influenced and family-controlled firms. The effect on the level of international scope for family-controlled firms with external managers was .498 ($p<0.01$) while the coefficient for family-influenced firms with external managers was .713 ($p<0.01$). The marginal effect of being a family-influenced firm with external managers was positive and equal to 0.215, confirming the positive and significant sign of the interaction term reported in Model 5.

6. DISCUSSION

Our results illustrate two important features. First, neither family ownership and control, nor the professionalization of management through the employment of external managers, can independently explain the international scope of family SMEs. Internationalization can only be maximized if both the management team and the

ownership structure are open to outside influence. Unless both equity capital and the management team are opened to outsiders, the full positive effects of external managers will not be enjoyed. For international scope, family SMEs may therefore consider an integrated and coherent corporate governance strategy in order to internalise external "bridging" social capital, and also open up their equity capital, thus reinforcing the role played by external managers.

In family firms, two forms of social capital - the family's and the firm's - coexist and may create governance and managerial dilemmas (Arregle at al., 2007; Lansberg, 1983). They may reflect two incompatible sets of values and norms, with the former oriented towards trust and strong social ties to assure the care and nurturance of family members, while the latter may follow an economic rationale to pursue efficiency (Lansberg, 1983). In family firms where the family group is dominant (in both ownership and management), the values and norms of the family institution may prevail over the organization's, constraining and eroding the efficient operation of family firms. In this type of firm, the presence of non-family managers/employees represents a context where inter-group heterogeneity and intra-group interaction within the family could create potential conflict (Arregle at al., 2007). In family firms where the family group is dominant and family social capital is strong, "…there is a tendency for the family to inappropriately capture the goodwill of external actors…" (Arregle at al., 2007, p. 87). This, in turn, can make non-family managers feel confined, thereby reducing their value to the firm.

In corporate governance terms, if family ownership is dominant, then classic Type II agency costs exist, and with a mixed family and outside management, Type I costs may also potentially arise (see Quadrant 4 of Table 1). An explanation for these results is that external managers may find themselves isolated within the strong relational ties of family-controlled firms, where family norms can be dysfunctional (Arregle et al., 2007). These norms may give rise to extra agency costs, tensions and misunderstandings between owners and external executives, especially with the family's bifurcation bias towards SEW objectives and greater loss aversion towards potentially risky/costly activities such as internationalization (Gomez-Mejia et. al, 2014).

Recent studies (Liang et al., 2014; Sciascia et al., 2012) report a curvilinear relationship between family ownership and internationalization. We did not estimate an optimal level of family ownership, but argue that the crucial factor is family

domination. With family ownership greater than 50%, the role for other "voices at the table" may be weaker, and the theoretically positive contribution of the bridging and bonding social capital of professional managers (once internalized within the boundary of the firm) may not have an effect on the scope of internationalization, and the margin between family and business objectives may blur. In this situation, family SMEs may favor non-economic goals, and the preservation of SEW may become a primary goal to the detriment of international scope. This result ties in with previous studies (e.g. Yang, 2010) reporting that high family ownership concentration may lead to a dominating influence that, in turn, could strongly attenuate any positive influence of external managers or a board with external members who promote internationalization (Calabrò et al., 2013).

On the other hand, for family-influenced SMEs with a majority of external capital, a positive relationship between external managers and family SMEs' international scope may prevail (see Quadrant 3 of Table 1), and interactions between family members and outsiders may contribute to the development of the family firm's social capital (Arregle at al., 2007). In other words, when a family firm allows outside investors to have a majority of shares, Type II agency costs and other negative effects of being a family firm are offset. At the same time, Type I agency costs may potentially benefit from an alignment between ownership and managerial diversity. In this case, while the positive effects of being a family firm remain, the presence of external capital and managers could combine synergistically, providing bridging and bonding social capital to promote international scope. When outside owners invest in a family business this means that the company is open not only to new investors but also to new managerial approaches and new ideas. Outside shareholders are extremely important since they play a signalling role: they are a concrete indication that the business is not just inward-looking but also open to external influences. The joint presence of external capital and external managers could attenuate the preservation of SEW and any tendency towards risk aversion in family SMEs, thus encouraging international scope. This result is in line with Sanchez-Bueno & Usero (2014) who found that the presence and ownership of a strategic investor as second largest shareholder in a family firm favored international diversification. However, the "openness" of family SMEs towards external capital must be coupled with the professionalization of management through the employment of external managers.

This research also offers a second important feature. It provides new evidence

that the family business world is heterogeneous and we respond to the plea that "…a theory of the family firm must be able to explain variations among family businesses" Chrisman et al. (2012, p. 267). Our results show that closely-held family firms are structurally different from family-influenced firms (Arregle et al., 2012), with different performance characteristics.

This could explain the inconclusive nature of the prior literature on family firm internationalization so far. Previous studies, failing to differentiate between family control and influence and/or between different levels of family ownership, could suffer from a specification problem, with a crucial omitted variable, when trying to explain the main determinants of internationalization. Thus, some conflicting prior results may have simply been the result of sample bias. If the sample analysed was dominated by family-controlled firms, then the role of external managers may have been under-estimated, or over-estimated in case of a sample dominated by family-influenced firms.

7. CONCLUSIONS

In a fresh attempt to understand the ownership conditions under which professional managers recruited from outside the family, Benavides-Velasco et al. (2013) favour internationalization by SMEs, this paper claims implications for 7.1 theory and 7.2 management practice.

7.1 Implications for Theory

Our paper contributes to the general SME internationalization literature by analyzing the role played by "external" influences (e.g. Agndal et al., 2008; Kontinen & Ojala, 2011a; Musteen et al., 2010; Prashantham, 2011; Zhou et al., 2007), in the form of professional managers recruited outside the family and their interaction with "internal" family ownership (e.g. George et al., 2005). A dominant view emphasizes a lack of market knowledge that constrains SME internationalization (e.g. Lu & Beamish, 2001). The extant family firm literature clearly demonstrates (Gedajlovic, Lubatkin & Schulze, 2004) that insider hiring at a managerial level can generally be detrimental. In this debate, an increasing number of scholars (Kotinen & Ojala, 2011a, 2011b; Musteen et al., 2010; Prashantham, 2011; Presutti et al., 2007; Yli-Renko et al., 2002; Zhou et al., 2007) have applied social capital theory to show how firms can overcome these knowledge constraints, by leveraging their networks of

relationships to access specific resources that promote internationalization. According to this view, externally-recruited professional managers have been considered particularly valuable because they provide additional specialized knowledge beyond the firm's boundaries that are extremely relevant to resource-constrained SMEs venturing across complex international business activities (e.g. Stewart & Hitt, 2012). By integrating social capital and corporate governance theories, and by employing the distinction between family-controlled and family-influenced SMEs, we showed that, in the context of family SME internationalization (Calabrò et al., 2013; Kontinen & Ojala, 2010, 2011a, 2011b; Liang et al., 2014; Merino et al., 2014; Pukall & Calabrò, 2014; Segaro, Larimo & Jones, 2014; Sciascia et al., 2012), externally-hired professional managers can only fully exert their potential if coupled with external ownership, allowing bridging and bonding social capital to emerge with the alignment of the positive effects of agency, stewardship and SEW processes.

This paper, focused on one strategy (i.e. the recruitment of non-family managers), viewed through the lens of social capital theory and governance (family ownership), can be seen as a response to the plea that "…future studies should attempt to provide different dimensions of learning orientation…" (Baum, Schwens & Kabst, 2015, p. 11), and suggests that the recruitment of outside managers may lie behind the "intense network contacts" reported to underpin internationalization (Baum et al., 2015).

We also claim that our paper may be considered in the wider context of theories of governance, strategy and performance, mainly based on large firms, where ownership structures are complex and information on strategies (e.g. the composition of executive boards and the degree of international diversification) is difficult to assess. In the relatively simplified ownership context of family SMEs it has been possible to investigate interactions between governance and strategy in relation to strategic outcomes. Our findings may have wider relevance in the context of large firms, and interactions between governance dimensions and other strategic decisions concerning not only executive hires but also organizational forms and joint ventures in host countries. Unfortunately, large firms tend to be complex in terms of governance and internal strategies are often unobservable. In this sense, family SMEs have provided a fruitful laboratory for identifying one key interaction.

Our paper also advances the literature in terms of the metrics of family SME internationalization. Previous studies have used FSTS as a measure of

internationalization. By using the entropy index (supported by similar results for FSTS) we align our study of SMEs with the most recent and advanced literature on international diversification (Gomez-Mejia, et al. 2010; Hitt et al. 2006; Majocchi & Strange, 2012; Sanchez-Bueno & Usero, 2014).

In addition, because of difficulties in obtaining a continuous measure of ownership levels in family firms, most contemporary research has frequently used a simple family/non-family SME distinction (Gomez-Mejia et al., 2014). Besides this family-influenced/family-controlled distinction, we checked our H2 for robustness, using a more fine-grained, continuous measure of family ownership, which we interacted with the presence of professional managers recruited from outside the family. This may also help to understand previously inconsistent empirical results (as explained above) and drive future research on this topic.

7.2 Implications for Practitioners

This research may have implications for practitioners, including family shareholders, outside shareholders, family managers and outsiders. Family-controlled SMEs needing extra resources for internationalization should be aware that either additional outside managers (Model 4, Table 5) or additional outside shareholders (Model 5, Table 5) on their own are not positively associated with internationalization. Knowledge of this outcome could deter outside investors from investing in firms that remain family-controlled: if family owners continue to control the firm, SEW theory would suggest that they are likely to suffer from bifurcation bias in favour of sources of utility other than dividends for all shareholders. Outside lenders aware of this outcome may also be wary about loans to family-controlled firms.

The positive relationship that we report between externally recruited managers and exporting has potential implications for managers and investors too. Providing that such exporting is profitable, the higher productivity of external managers can earn them higher rewards and job security, or generate higher returns for investors, or both.

For family SMEs themselves, the novel implication of this study is that if they want to derive full value from externally-recruited managers, they should simultaneously concede majority ownership control. Outside managers, investors and lenders may prefer to seek involvement in firms with external managers, and where

family ownership is less than 50%. Again, the implication for family owners and managers in family-controlled firms without external managers is that they probably need to consider whether the trade-off between the benefits of outside shareholders *and* managers together is worth possible losses of SEW.

7.3 Limitations and Further Research

Despite its theoretical and practical implications, however, this study also has four main limitations that could constitute opportunities for further research and refinement. First, our empirical setting is Italy, a single country with a large number of family SMEs that feature weak protection of minority interests (Mazzi, 2011). It has been shown that the legal protection of minority shareholders (Djankov, La Porta, Lopez-de-Silanes & Shleifer, 2008) determines the effect of family ownership. Consequently it could be that the positive effects of outside shareholders are particularly strong in this institutional setting. Nevertheless, international comparisons, including different corporate legal systems, beyond Italy could validate our findings. For example, measures of cultural/institutional distance could identify other influences.

Second, our associations identify, for manufacturing SMEs only, what effect external influences have on family SMEs' international scope, but cannot conclusively establish why. Meanwhile, however, some case studies are consistent with our associations at a micro-level. Hagen & Majocchi (2014) report the case of Luxottica, a small, local, Italian manufacturer of frame components in the 1960s that evolved into the world leader in the eyewear and sunglasses business, owning iconic brands such as Ray-Ban and Oakley among others. International expansion by Luxottica was evidently triggered by the decision to introduce professional managers. Interestingly, the first strategic decision of the new, outsider-influenced board was to obtain a listing on the NYSE and this provided the funds for internationalization as well as a new governance structure. Additional anecdotal evidence from around the world (e.g. Graves & Thomas, 2006) also refers to the need for external managerial capabilities and externally generated funds as conditions for international expansion of family firms. However, we need further qualitative research on this topic to identify precisely *how* external influences enhance internationalization.

Third, although our study did have a temporal element to the extent of using lags to identify causation, it can add little to the extant literature on pathways to

internationalization, e.g. traditional (incremental) internationalizing firms, “born globals”, “born-again globals” (Tuppura, Saarenketo, Puumalainen, Jantunen & Kyläheiko, 2008), and “born regionals” (Baum et al., 2015). At the same time, this limitation represents a research opportunity, noted below.

Finally, a lack of data meant that we could not control for different internationalization strategies. Further research may also establish the levels of education and the nationalities of external managers as well as their previous work experience.

Besides these weaknesses, however, we suggest new avenues for research. For SMEs, it could be important to discover which particular functional expertise (e.g. marketing, administrative, finance, operations, etc.) and/or skills (e.g. foreign language ability) is contributed by externally-recruited managers. Approximately 50% of internationalizing SMEs are traditional, incremental internationalizers (Baum et al., 2015) and Tuppura et al. (2008) emphasize the importance of accumulating expertise (especially market knowledge) for these firms.

This could complement our focus on external hires. Besides this strategy of external hiring, it would also be interesting to establish how other strategies (e.g. external borrowing and managers recruited from countries that are targets for internationalization) may interact with ownership characteristics.

Another interesting research avenue could involve investigating histories of inside and outside managers working together in the decision-making process (Dierickx & Cool, 1989) and how they can facilitate the emergence of effective norms and values, thereby strengthening bonding and bridging social capital and thus favoring successful venturing into foreign markets.

Beyond SMEs, the application of social capital theory to the context of SME internationalization suggests that it may also be applied to larger firms, with new investigations along the lines suggested by Toms & Filatotchev (2004), possibly embracing human as well as social capital. Finally, it should be noted that, of course, there is no guarantee that any increased scale or scope of internationalization is a “good thing” (Brouthers et al., 2009), and further research should be able to complete the governance-strategy-performance sequence by adding SMEs’ financial performance to the analysis.

Table 1: The consequences of ownership (family-influenced vs family-controlled) and management involvement (family managers only vs family and external managers)

		Family ownership	
		Influenced (<50%)	*Controlled (>50%)*
Management	**Family Only**	**Quadrant 1** **Agency costs (Type I)** (+) *family managers aligned with family owners* (-) *but not with majority outside shareholders* **Agency costs (Type II)** (-) *minority family shareholders find support from family managers to exploit outside shareholders* **Stewardship/SEW** (+) *stewardship and SEW moderated by majority outside shareholders* (+) *lower loss aversion* (+) *less bifurcation bias in favour of family SEW* (+) *access to external capital* (-) *but less patient capital* (-) *managerial under-training (Carnegie effect), nepotism, entrenchment*	**Quadrant 2** **Agency costs (Type I)** (+) *family managers aligned with family owners* **Agency costs (Type II)** (-) *majority family shareholders find support from family managers to exploit minority outside shareholders* **Stewardship/SEW** (-) *emphasis on stewardship and SEW: high loss aversion* (-) *Bifurcation bias in favour of SEW* (-) *limited access to capital* (+) *but more patient capital* (-) *managerial under-training (Carnegie effect), nepotism, entrenchment*
	Family and External	**Quadrant 3** **Agency costs (Type I)** (-) *weaker incentives for self-monitoring by family managers* (+) *managerial diversity aligned with ownership diversity* **Agency costs (Type II)** (+) *family and outside shareholders find some support from family and outside managers. More "voices at the table" reduce agency type II costs* **Stewardship/SEW** (+) *stewardship and SEW moderated by majority outside shareholders and outside managers* (+) *lower loss aversion* (+) *low bifurcation bias in favour of SEW* (+) *access to outside capital* (-) *but less patient*	**Quadrant 4** **Agency costs (Type I)** (-) *potential alignment problems between family shareholders and outside managers* **Agency costs (Type II)** (-) *majority family shareholders find support from family managers to exploit minority shareholders and outside managers* **Stewardship/SEW** (+) *stewardship and SEW moderated by external mangers* (-) *higher loss aversion* (-) *bifurcation bias in favour of SEW* (-) *limited access to capital* (+) *but more patient*

Note: The signs (+/-) are from the agency perspective of economic efficiency.

Table 2: Variable names, constructs and measurements

Variables name	Constructs and measurements	Source
DEPENDENT		
Entropy	Scale and scope of internationalization (export dispersion)	Gomez-Mejia et al. (2010); Majocchi & Strange (2012)
INDEPENDENT		
External managers	Dummy variable = 1 if firm has hired external managers in addition to family managers	Adapted from Arregle et al. (2012); Majocchi & Strange (2012)
Family influenced	Dummy variable = 1 if family ownership is less than 50%	Sirmon et al. (2008); Arregle et al. (2012)
*Fam inf*Ext mng*	Interaction *Family influenced* × *External managers*	
Family ownership	Percentage of family ownership (%)	Graves & Thomas (2006); Fernandez & Nieto (2006)
*Fam own*Ext mng*	Interaction *Family ownership* × *External managers*	
CONTROL		
Age	Number of years since foundation	Gomez-Mejia et al. (2010)
Size	Natural log of number of employees	Verwaal & Donkers (2002)
Traditional/Scale-intensive/Specialized suppliers/Science-based	Dummy variables for Pavitt industrial sectors	Cerrato & Piva (2012)
North-West/North-East/Centre/South and Islands	Dummy variables for firm's location within Italy	Basile (2001)
Group	Dummy = 1 if the firm is part of a business group	Cerrato & Piva (2012)
R&D	Number of employees in R&D over total number of employees (%)	Hoffman et al. (1998)
ROI	Return on investment	Gomez-Mejia et al. (2010)*
Reg_sales	Sales in EU over total sales (regional export intensity) (%)	Adapted from Hashai (2011)

Note 1: *Gomez-Mejia et al. (2010) used ROA as a measure of performance.
Note 2: All independent variables refer to 2003, the dependent variable (Entropy) refers to 2006.
Note 3: The variable *External managers* is also used as *moderator* in Models 5 and 6 of Table 5.

Table 3: Descriptive statistics of binary variables

		Freq	**Perc**
External managers	0=No	290	69.54
	1=Yes	127	30.46
Pavitt	Traditional	224	53.72
	Scale-intensive	62	14.87
	Specialised-suppliers	118	28.30
	Science-based	13	3.12
Area	North West	156	3741
	North East	125	29.99
	Centre	80	19.38
	South & Islands	56	13.43
Group	0=No	367	88.01
	1=Yes	50	11.99

Table 4: Descriptive statistics and correlation of continuous variables

	Mean	**SD**	Age	Size	R&D	ROI	Reg_sales
Age	31.61	23.79	1.				
Size	4.01	.719	0.143***	1.			
R&D	.035	.590	0.038	0.005	1.		
ROI	15.98	28.81	-0.0982**	-0.2184***	0.0644	1	
Reg_sales	51.02	38.29	0.0617	0.0957*	0.0349	0.0010	1

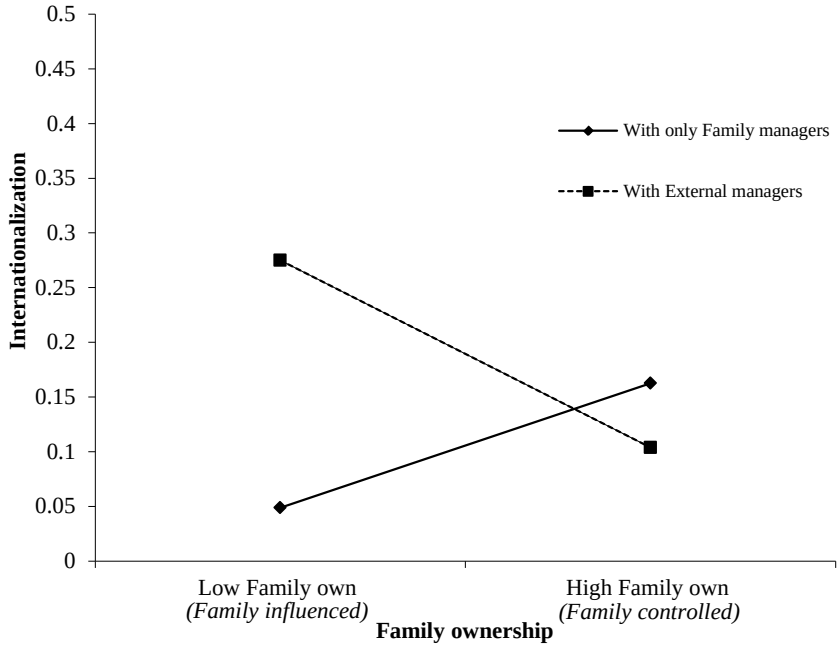
Note: *** p<0.01; ** p<0.05; * p<0.1

Table 5: Tobit regressions results on entropy

Entropy	Model (1)	Model (2)	Model (3) Family-influenced	Model (4) Family-controlled	Model (5)	Model (6)
Age	0.000631	0.000539	0.00129	-0.00338	0.000479	0.000452
	(0.00120)	(0.00119)	(0.00137)	(0.00228)	(0.00119)	(0.00119)
Size	0.232***	0.211***	0.258***	0.137**	0.218***	0.221***
	(0.0419)	(0.0436)	(0.0552)	(0.0691)	(0.0434)	(0.0436)
Scale-intensive	-0.0205	-0.00938	0.0378	-0.0935	0.00197	-0.00942
	(0.0850)	(0.0849)	(0.106)	(0.136)	(0.0845)	(0.0842)
Specialized suppliers	0.231***	0.223***	0.221***	0.193*	0.230***	0.214***
	(0.0674)	(0.0674)	(0.0810)	(0.113)	(0.0671)	(0.0670)
Science-based	0.00581	0.00713	-0.382	0.205	0.0214	0.00470
	(0.174)	(0.173)	(0.287)	(0.231)	(0.172)	(0.178)
North-East	-0.0860	-0.0786	-0.204**	0.0649	-0.0781	-0.0505
	(0.0701)	(0.0701)	(0.0912)	(0.108)	(0.0699)	(0.0700)
Centre	-0.0845	-0.0778	-0.0619	-0.210	-0.0855	-0.0872
	(0.0807)	(0.0806)	(0.0936)	(0.146)	(0.0802)	(0.0800)
South and Islands	-0.0713	-0.0631	-0.119	-0.0270	-0.0708	-0.0573
	(0.0939)	(0.0937)	(0.113)	(0.155)	(0.0930)	(0.0945)
Group	0.158*	0.134	-0.0164	0.317**	0.147*	0.113
	(0.0870)	(0.0880)	(0.126)	(0.122)	(0.0884)	(0.0898)
R&D	1.418***	1.398***	1.527***	1.415	1.339***	1.408***
	(0.488)	(0.487)	(0.563)	(0.950)	(0.484)	(0.481)
ROI	0.000730	0.000771	7.49e-05	0.000605	0.000729	0.000768
	(0.00103)	(0.00102)	(0.00141)	(0.00149)	(0.00102)	(0.00102)
Reg_sales	0.00457***	0.00455***	0.00472***	0.00375***	0.00441***	0.00459***
	(0.000771)	(0.000768)	(0.000966)	(0.00122)	(0.000766)	(0.000769)
External managers		0.105*	0.192**	-0.0550	-0.0743	0.421***
		(0.060)	(0.0789)	(0.110)	(0.101)	(0.143)
Family influenced					-0.0754	
					(0.0698)	
*Fam inf*Ext mng*					0.284**	
					(0.123)	
Family ownership						0.00132
						(0.00142)
*Fam own*Ext mng*						-0.00643**
						(0.00251)
Constant	-0.846***	-0.793***	-0.980***	-0.346	-0.764***	-0.894***
	(0.186)	(0.188)	(0.233)	(0.307)	(0.190)	(0.207)
Pseudo R^2	.1424	.1456	.2113	.1277	.1523	.1521
Obs. (left-censored)	417(114)	417(114)	254(68)	163(46)	417 (114)	408 (110)

Note: Standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1

Figure 1: Interaction between Family ownership and External managers on Internationalization



Note: Constant term set equal to 0. Uncentered variables.

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